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Pensions & Investment Age

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The GEIC fund has completed purchase of the Hyatt Regency in Hilton Head, S.C.

General Electric cuts realty allocation 20%

By Alan Krauss

STAMFORD, Conn. — The $13.3 billion General Electric Co. pension fund has reduced its real estate holdings 20% to 25% in response to a sluggish, uncertain market.

The pension trust has reduced its real estate exposure by $300 million to $400 million during the past 18 months in the course of restructuring the portfolio and "due to market conditions," said Joel R. Wilson. Mr. Wilson is senior vice president of General Electric Investment Corp., the giant manufacturing company's pension investment subsidiary, and manager of its real estate investment activities.

Real estate

The trust now has about $1.6 billion, or 12% of assets, in property investments.

"We have not diminished our feeling that real estate is a viable and key part of our enhancement activities," Mr. Wilson said, referring to GEIC's distinction between "core" pension investments — common equity and fixed-income portfolios — and "enhancement arenas" such as real estate, corporate private placements and venture capital.

The trust is restructuring its portfolio by eliminating non-equity real estate investments, Mr. Wilson said, citing the recent sale of $600 million in non-participating mortgages to Salomon Brothers Inc.

"At the same time we have reduced the absolute number of dollars going into real estate, (and) deteriorating market conditions (have driven) the sales of other properties," he noted.

Noting property prices have been flat for most of the past 18 months, Mr. Wilson attributed the muddled condition of the market to several other factors. While the slowdown in syndication activity has been offset by continued buying by the large insurance companies, office markets are overbuilt, there is continued concern about tax reform and "the general perception of the real estate markets" is marked by confusion, he said.

"It's a very complicated picture right now," he said. "There is much uncertainty ... about how these factors will interact."

GEIC is highly regarded throughout the industry

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Wheeling-Pitt rivals push for change on PBGC liability rule

By Trudy Ring

PITTSBURGH — At least two competitors are lobbying, and others are complaining, that Wheeling-Pittsburgh Steel Corp. should be liable for some of the huge unfunded pension liability it is dumping on the Pension Benefit Guaranty Corp.

Wheeling-Pitt, one of several financially strapped steel companies with underfunded pension plans, would have a competitive advantage if it is able to rid itself of its estimated $440 million unfunded liability, officials of other steel firms say.

National Intergroup Inc., Pittsburgh, is lobbying for modifications in proposed PBGC legislation in an attempt to make it applicable to the Wheeling-Pitt situation, a spokesman confirmed.

Representatives of Cyclops Corp., also of Pittsburgh, have met with the PBGC and members of Congress concerning the legislation, a spokesman said. Also, Cyclops' president has denounced Wheeling-Pitt's termination attempt in the daily press.

Officials of some other steel companies said they believe allowing Wheeling-Pitt to get rid of unfunded liabilities while continuing in business is unfair to the rest of the industry, but added they aren't aware of specific lobbying efforts. The chief executive officer of U.S. Steel Corp. has labeled the termination effort "industrial welfare."

Wheeling-Pittsburgh officials had no comment.

If the pending PBGC legislative package is adopted and made retroac-

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L.A. County hires 5 for real estate

By Steve Hemmerick

LOS ANGELES — Los Angeles County Employees' Retirement Association trustees have decided to make the fund's first significant move into real estate, hiring five real estate managers and committing at least $100 million to them.

The county fund hired: John McMahan Associates Inc., San Francisco; The Prudential Asset Management Co., Newark, N.J.; Heitman Advisory Corp., Chicago; Goldman, Sachs & Co., New York; and Security Capital Real Estate, New York.

In hiring the five managers with complementary styles, the trustees sought not only to diversify into real estate, but to diversify within real estate itself, said Charles Spencer, fund manager.

By the end of the year, the retirement association could commit another $50 million, bringing the total investment to $150 million. Mr. Spencer said trustees could choose a sixth manager from

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Pipelines facing asset flood

By Fred Williams

DALLAS — Officials of six natural gas pipeline companies, all subjects of mergers and acquisitions, are grappling with how to allocate more than $1.5 billion in pension assets.

They also may have to wrestle with the disposition of surplus assets in overfunded pension plans if the plans are terminated.

Should a termination occur, the role of the regulatory agency might become a factor in deciding who gets the surplus — the corporation or the customer.

Natural gas pipeline companies have been involved in mergers totaling $5.6 billion so far this year. Among them:

- Coastal Corp., Houston, acquired American Natural Resources Co., Detroit, for about $2.3 billion.
- InterNorth Inc., Omaha, Neb., merged with Houston Natural Gas Corp., in a deal valued at about $2.1 billion.
- MidCon Corp., Chicago, is in the final stages of acquiring United Energy Resources Inc., Houston, in a deal estimated at about $1.2 billion.

The acquiring and acquired companies had overfunded pension plans with total assets of about $1.53 billion at the end of 1984 and excess assets of $478.8 million.

Pension executives say plan design and eventual disposition of assets remains to be determined, but Curt Launer, pipeline industry analyst for L.F. Rothschild, Unterberg, Towbin, New York, believes the overfunding is integral to the pipeline mergers and acquisitions.

"The overfunded status of the pension plans was not the thing that got it started, but was a big factor in keeping it going. Overfunded pension plans, unused investment tax credits and tax loss carryforwards all were very important considerations," he said.

While none of the pipeline companies in the first round of mergers has filed to terminate any of the plans, if the industry follows the pattern established by oil companies, banks and thrift institutions, there could be a series of termination notices by pipeline

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Defined contribution highlighted

Oil field service and products division workers for Halliburton Co. The Dallas company's defined contribution plan is one of several profiled in the special section beginning on page 37.

Refinancing cuts liabilities

Harvester considers leasing

By Barry B. Burr

CHICAGO — International Harvester Co. is exploring leasing as one way to use $1.4 billion of tax loss carryforwards after it received renewed vigor by putting together a widely praised refinancing package that includes cutting by more than half its $900 million in unfunded pension liabilities.

John R. MacLean, assistant treasurer, said the carryforwards represent an opportunity to shelter income from taxes.

As of Oct. 31, 1984, the close of its last fiscal year for which data are available, Harvester had $972 million of domestic and $442 million of foreign carryforwards available to reduce future taxable income. Of the total, $319 million is available through 1992, the rest thereafter.

"We are are not looking to make acquisitions," Mr. MacLean said. "We aren't going to use cash to buy other companies to use" the carryforwards."

Before putting together its refinancing, Mr. MacLean said Harvester momentarily considered turning over its unfunded pension liabilities to the Pension Benefit Guaranty Corp.

"We considered it for a nanosecond," he said.

But such an action undoubtedly would have triggered a bankruptcy, with the PBGC asserting claims on the company's assets to try to cover the liabilities, he added.

One area the company the company is looking at is leasing. He said Harvester is considering buying leases that have lost their tax write-off value for their existing holders. Firms in that position "would just as soon not have the leases," Mr. MacLean said.

"It's a very complicated deal," he added. "I assure you it's a very exploratory area."

Harvester, whose business now is more than 90% truck manufacturing, sold its name along with its agricultural division to a unit of Tenneco Inc. last January and will adopt a new name next year.

James C. Cotting, vice chairmand and chief financial officer, said the voluntary refinancing is designed to reduce the company's unfunded pension liabilities by about $500 million and to improve its capitalization by changing $200 million in private floating-rate debt of its parent and credit unit for public long-term debt. In addition, the improved credit picture will enable its International Harvester Credit Corp. unit to issue commercial paper for the first time in three years.

Mr. Cotting said the refinancing would have no immediate effect on Harvester's negative net worth. Also, the company still will have about $800 million in long-term debt.

With Harvester's improved picture, Charles V. Bromley, analyst with Duff & Phelps Inc., Chicago, called the negative net worth "an academic thing. Its cash flow is good, so it doesn't matter."

However, he added, Duff & Phelps wasn't immediately going to change Harvester's credit rating of 16, its second worst rating.

An official at Prudential Insurance Co. of America, Newark, N.J., praised the move. Prudential is a long-time lender to Harvester and potentially its biggest shareholder with interests that could give it ownership of 10% of the company.

Harvester is taking $350 million in equity out of its credit subsidiary to use for the pension plan. Harvester will use the cash to set up a dedicated bond portfolio yielding an estimated 12%.

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More than 90% of Harvester's business now is truck manufacturing.

The *P&I Age* monthly indexes track the changes in the Standard & Poor's 500 stock index, the Russell 3000 stock index, the Ryan Index of fixed-income securities and the Shearson Lehman Government/Corporate bond index.

***P&I Age* October indexes**

	Latest mo.	Year to-date	Trailing 12 mos.
S&P 500	4.6	11.6	19.4
Russell 3000[1]	4.6	18.2	19.8
Ryan Index[2]	2.1	16.8	20.6
SLAE Gov't./Corp.[2]	2.0	15.0	18.7

Source: Rogers, Casey and Barksdale Inc.

[1]Frank Russell Co. [2]Fixed income

PBGC adopts get-tough approach

By Joel Chernoff

News analysis

WASHINGTON — The agreement to collateralize The LTV Corp.'s $183 million funding waiver shows the Pension Benefit Guaranty Corp. is evolving into a hard-nosed, high-profile agency from one that once was obscure outside pension circles.

Although the agency was created in 1974, it didn't begin to garner national attention until the early 1980s, with such big cases as International Harvester Co., Rath Packing Corp., Facet Enterprises Inc., Armco Inc., Wheeling-Pittsburgh Steel Corp. and others.

Its get-tough stance was most apparent in getting LTV of Dallas to agree to the collateralized waiver.

In the process, LTV officials privately condemned part of the PBGC's method of operation, accusing the federal agency of leaking key information to the press.

In particular, stories in nationwide publications saying the PBGC was seriously considering seeking involuntary termination of LTV's

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3 plans tap venture cap

By Trudy Ring

Three venture capital funds recently have drawn investments from pension funds.

The pension funds of Independent Insurance Group, Jacksonville, Fla., and L.M. Berry & Co., Dayton, Ohio, made commitments to the Santa Fe Private Equity Fund II, Santa Fe, N.M., which will invest primarily in health care companies.

The Michigan State Employees' Retirement Systems invested in two venture funds, Accel Telecom of Princeton, N.J., which will invest in telecommunications and data communications companies, and New Tech Ventures, San Francisco, which will specialize in industrial technology.

Independent Insurance Group's $80 million pension fund put $750,000 into the Santa Fe fund, said Tom Weaver, president of Independent Investment Advisory Services Inc., the subsidiary handling the pension assets.

L.M. Berry, with $40 million in pension assets, invested $500,000 in the Santa Fe fund, said Donald T. Zimmer, treasurer.

The International Business Machines Corp. pension fund, Stamford, Conn., also reportedly is an investor in the fund, but an IBM official said it is company policy not to discuss investment matters with the press.

Both Mr. Weaver and Mr. Zimmer said one reason for their investments was the expertise of A. David Silver, managing general partner of the fund. Mr. Silver, a venture capitalist since 1967, had raised another Santa Fe fund in 1983. It also invested in health care companies, as well as computer-related companies.

For the new Santa Fe fund, Mr. Silver has raised about $15 million to date. He said he expects to raise $35 million, with the fund closing Jan. 31.

About 30% of the capital raised to date has come from pension funds, Mr. Silver said. Much of the remainder has come from the general accounts of insurance companies, he said.

Mr. Silver said he expects to

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Guidelines survive INTERCO lawsuit

By Joel Chernoff

The Reagan administration guidelines on asset reversions from pension plan terminations survived their first legal challenge when a federal judge last week threw out a suit brought by INTERCO Inc. of St. Louis.

"We're very pleased," said Kathleen Utgoff, executive director of the Pension Benefit Guaranty Corp. "We're more than pleased."

In his ruling, U.S. District Court Judge John Nangle of St. Louis held the PBGC is owed great deference in determining whether a termination has taken place.

The judge ducked the controversial issue of whether the administration's guidelines are valid under law.

"This court agrees with the PBGC that the guidelines are irrelevant to the issue in this case. It is clear to this court that Title IV of (the Employee Retirement Income Security Act) grants the PBGC the authority to deny recognition of INTERCO's termination action even if the guidelines had never been issued," the judge wrote.

An attorney for INTERCO said the company is reviewing the decision and does not know whether it will be appealed.

Roger Thomas, pension counsel for the House Select Committee on Aging, said that because the court did not appear to rule on the merits of the termination guidelines, their legality still is in doubt.

A separate lawsuit challenging the spinoff/termination of United Air Lines Inc.'s pilots' plan is in litigation, in a case that might affect the guidelines' legality (*Pensions & Investment Age*, Aug. 19).

A lot was riding on the INTERCO case. Employers have taken advantage of methods allowed under the guidelines to recapture billions of dollars in surplus assets while still providing defined benefit plans for their current employees.

The guidelines, adopted in May 1984 after months of debate by the PBGC and the Departments of Labor and Treasury, allow companies to recapture surplus assets through either a spinoff/termination or a termination/re-establishment.

In the former, the original plan is split into two parts with the excess assets placed in one of the plans, which is later terminated, enabling a recapture. In the latter, the entire plan is terminated, and a similar plan replaces it.

Key to the guidelines was a requirement that employers fully vest all employees in the original

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New listings' price surge studied

By Barry B. Burr

Index fund managers increasingly are paying dearly — and sometimes unnecessarily — to acquire stocks newly listed on the Standard & Poor's 500 index, a study by two University of Southern California academics shows.

The study shows a sudden surge of trading volume and an abrupt increase in the stock price the first day after a new S&P 500 listing is announced. The extraordinary demand and price continue for several days and then generally fall back, although their average volume remains higher than the level prior to the announcement.

In their study, Lawrence E. Harris and Eitan Gurel, both assistant professors of finance and business economics, attribute the sharp rise in price to the surge of buying by institutional investors to add the newly listed stocks to their index fund portfolios.

Impact of listing stock in S&P 500 index[1]

Period	Trading volume[2]	Price changes[3]
Monday	89%	0.01%
Tuesday	91	−0.13
Wednesday[4]	95	0.01
Thursday	281	3.13
Friday	162	0.09
Monday	151	−0.21
Tuesday	123	0.02

[1] There were 84 additions to S&P 500 between 1978 and 1983
[2] Relative to previous averages adjusted for market activity
[3] Relative to price change of market as whole
[4] Stocks are added to S&P 500 on Wednesdays after the market closes

Source: Lawrence E. Harris and Eitan Gurel

Moreover, they say the steep rise in volume and price for the newly listed stocks is increasing as index funds grow in size and exert more influence on stock prices of the S&P 500 index.

Index fund assets run by managers increased to $46.6 billion in 1984 from $9 billion in 1980, according to a survey (*Pensions & Investment Age*, April 1). Other estimates put the amount now at $60 billion and, when pension plan in-house index portfolios are included, at $100 billion.

Managers at several major index funds, while generally agreeing with the USC study, contend the findings don't necessarily apply to them because of various strategies they use to ease the price impact.

Indeed, Mr. Harris said, "Certainly the smarter ones (managers) are holding back somewhat until the price falls back" before buying.

Managers said the strategies some of them use to buy newly listed S&P 500 stocks become a way of differentiating the seemingly uniform index funds.

Patricia C. Dunn, vice president at Wells Fargo Investment Advisors, San Francisco, said the price impact of acquiring newly listed S&P stocks "is an issue every indexer has to deal with effectively and every index client has to be concerned with."

"It's a competitive issue among indexers. It's one of the few aspects of an index on whether you can do a better job than another indexer," she said.

At Northern Trust Co., Chicago, Mike N. Alex, second vice president, said, "There is no need to run out and buy that stock immediately.

"It becomes a timing play. I tend to stay away from a stock for one or two months, until it comes back down to a better price."

Such a strategy, he added, "could be a potential problem, if it is a big stock. But in that case, we would buy the stock that (first) day and pay whatever penalty there is."

Ms. Dunn said, "If you're an indexer, you have to work your trading with this in mind. Otherwise you will give up some return."

In one approach to dealing with S&P 500 additions, Ms. Dunn said, Wells Fargo sets up limited orders.

"We take our time to acquire the stock," she said, purchasing the stock so long as the price impact is no more than one-half basis point after market movement adjustment.

Also, for clients with other portfolios with Wells Fargo, she might sell S&P stocks to their index accounts "with no market impact."

At Great American Core Investors Inc., Tarrytown, N.Y., Robert A. Windsor, vice president, said the price managers pay for the stocks "really would depend on what type of index fund you are running."

"If you are buying all 500 stocks, then you have to buy that stock," he said.

Unlike Wells Fargo, Great American runs a sample index of 275 to 300 stocks, selected to track the S&P 500.

Few managers use samples, said Ravi Aiyer, director of research at Paribas Asset Management, New York. Most indexers buy all or close to all 500 stocks, generally eliminating bankruptcy candidates.

Northern Trust holds 444 stocks, screening stocks for financial viability, Mr. Alex said.

Great American buys all the big S&P 500 stocks and a sampling of the smaller ones. "You would have to buy a very large stock, because its movement would have a big impact on the index," Mr. Windsor said.

The managers, among others, noted pension executives often don't raise the issue of purchasing strategies for newly listed stocks when selecting index funds.

In attributing the price rise to purchases by index fund managers, Messrs. Harris and Gurel say, "It is unlikely that changes in the

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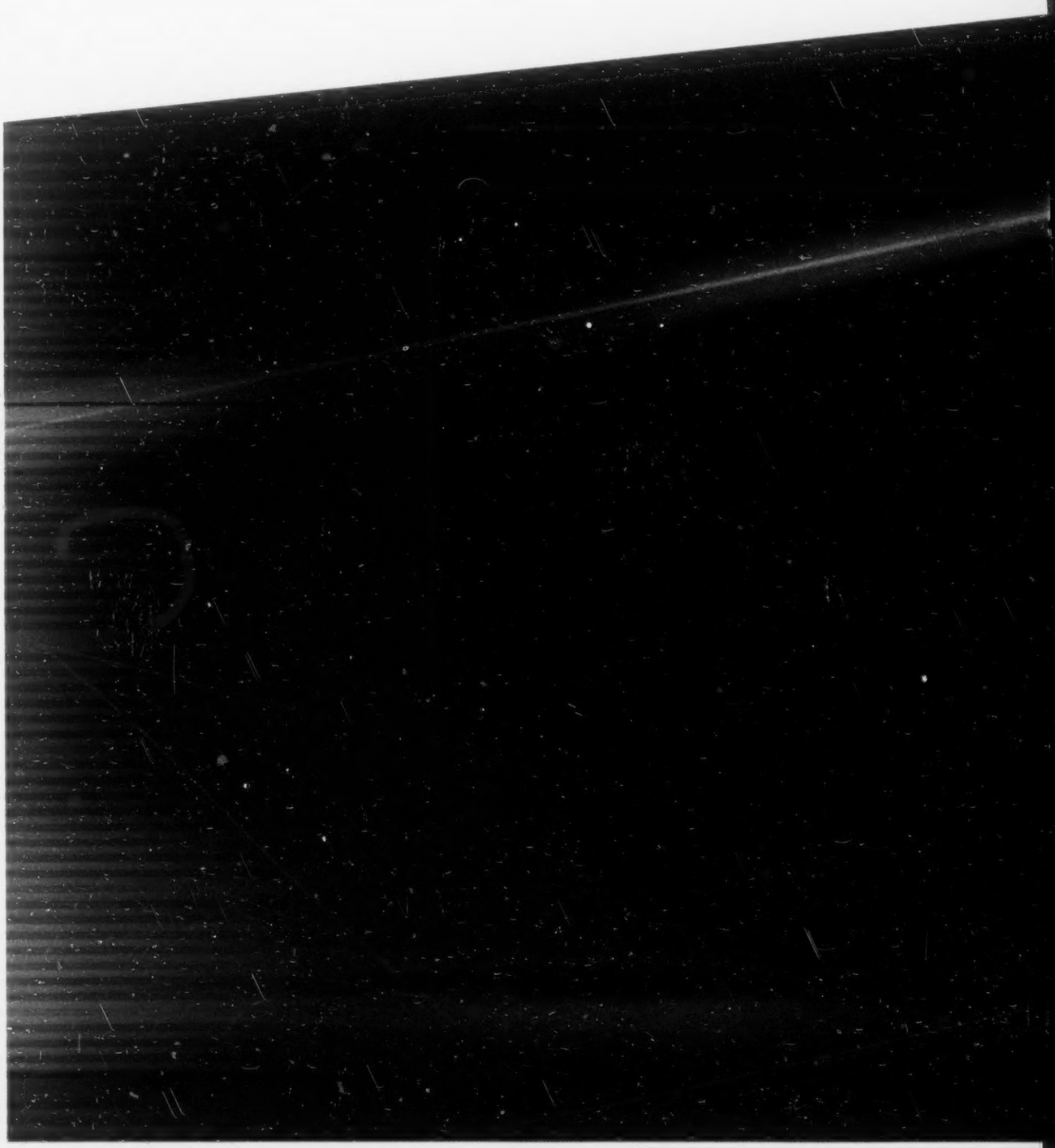
Now business



New listings . . .

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composition of the S&P 500 list convey new information" about the companies that would cause an upward valuation of the stock prices.

"When a stock is added to the list, they (index managers) may buy it where previously they would not," the two academics wrote.

Mr. Harris said, "All it (the rise) can be is price pressure in buying the stocks." He and his colleague call their findings the price-pressure hypothesis.

Standard & Poor's Corp. customarily announces replacement listings on Wednesdays after the close of the stock market.

Messrs. Harris and Gurel studied the 211 additions to the index between 1973 and 1983 and found the volume and price surges were increasingly more pronounced in recent years.

"Volume and price effects grew in strength through the sample period because index funds grew," they wrote.

In looking at the 50 new listings between 1981 and 1983, Messrs. Harris and Gurel found in the trading Thursdays that volume, adjusted for market volume, rose slightly more than an average of 340% from each stock's volume eight weeks before the announced inclusion and price rose 3.25% over the average price rise in the market as a whole.

While volume and price increases begin to decline after the first Thursday of trading, slowly moving back to preannouncement level, volume continues to stay above its prelisting level. Their study suggests, "Inclusion on the S&P 500 list permanently increases a security's trading volume."

For active managers, the new listing can bring a quick and tidy profit, as they sell shares to passive managers, said Mr. Harris and others.

Mr. Harris suggested the volume and price increases could be even more pronounce than the study shows.

"I think if all the index funds bought (the stock) on the first day (of trading after the announcement) the results would be more dramatic," he said. "I think some do defer the purchase of the stock."

When Mr. Windsor wants to include a newly listed stock in Great American's sample index, he said, "I typically will not run out and buy a stock the next day" after it is listed. "I wait for the price to come back in line."

The impact of a stock on tracking the S&P 500 generally "isn't critical enough to run out and buy the stock the next day and run up the stock price," he added.

"A big company might be 1% of the S&P. If the stock makes a 10% move (in price), then you have a 10-basis point move in the index — a large move in the index."

But during a year, such tracking errors might add up, with an average of 20 annual changes in the S&P 500.

The issue of sampling or indexing turns in part on the price impact of acquiring newly listed S&P stocks.

One criticism of having a full or nearly full 500-stock index against a sampling "is that you are buying high," said Ms. Dunn.

"But to counter that you have to look at the returns of full cap weighted funds vs. sample funds. Full cap weighted funds have been closer to the S&P than sample funds," consultants say.

But sample funds have advantages, too. "Custodian, monitoring and trading costs should be lower," said Paribas' Mr. Atyer. "But the sample will not track every major move in the S&P.

"The problem with sampling is no one has come up with a sample to minimize tracking error."

Wayne H. Wagner, vice president of Wilshire Associates, Santa Monica, Calif., said his investment and consulting firm has surveyed funds of 100 to 500 stocks and found the larger the holdings, the smaller the tracking error. ■

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Early retirement incentive offered by 7% in 1984

CHICAGO — Early retirement incentive offers in 1984 remained at a relatively low level for the second consecutive year, according to Charles D. Spencer & Associates' third annual survey.

Slightly more than 7% of the 171 employers who responded to the survey opened the early retirement window in 1984, the same as in 1983.

In 1982, however, more than 25% of the survey's respondents reported making incentive offers.

According to Spencer's report on the survey, the drop in retirement incentives can be traced to the recession of the early 1980s. Early retirement proposals became a solution for employers feeling the pinch of increased levels of competition and the heady pace of technological advancement.

Most of the employers surveyed offered early exit inducements to thin the ranks of longer-service employees without resorting to layoffs or involuntary terminations. Other reasons cited were "to provide more opportunities for promotion" and "payroll cost savings."

The retirement inducement offered most frequently by the survey respondents was some form of monthly supplement to the pensions benefits, or a bridging payment. Other incentives included actuarially unreduced pension, one-time cash payment, salary continuation at a reduced level and added service credit for faster vesting.

The majority of the offering employers instituted corporatewide benefits changes. More than half initiated health-care changes and established 401(k) plans.

Most of the offering employers aimed their incentives at people in their 50s.

As a class, the group of eligibles was somewhat younger than the group eligible in 1982 and 1983. In 1983, for instance, more than half of the offering employers focused on people at least age 60. ■